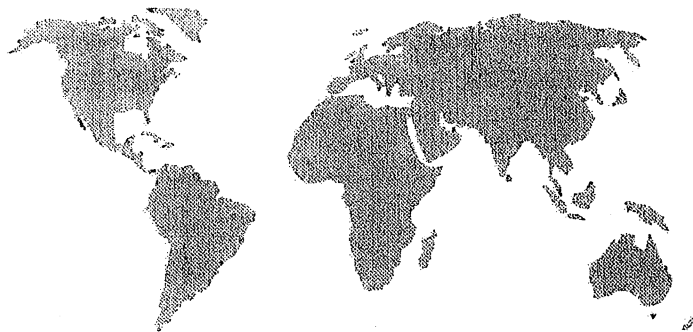


# Viewpoints



## Why Not Des Moines?

### A Fresh Entry in the Subpart F Debate

by H. David Rosenbloom

*H. David Rosenbloom is a member of Caplin & Drysdale, Chtd, in Washington and director of the International Tax Program at the New York University School of Law.*

**A**fter the 15 July hearings on "U.S. Tax Policy and Its Effect on the International Competitiveness of U.S.-Owned Foreign Operations," U.S. Senate Finance Committee Chairman Charles E. Grassley, R-Iowa, posed the following written questions to witnesses:

Company X manufactures widgets in the United States for sale in the United States and abroad. It forms a subsidiary, Y, in a zero-tax jurisdiction such as Bermuda to serve as a trading company. Y hires 200 persons in Hamilton. Widgets are sold by X to Y for 100, and Y resells the widgets, without changing them, for 125 to unrelated parties in the United States and the rest of the world. The transfer price from X to Y is defensible. The 25 earned by Y is attributable to economic functions that Y performs in Bermuda. Should the United States tax that 25? Why or why not?

Those are good questions. And this is an excellent way to relaunch a debate on what should be

done to, or about, the main U.S. antideferral statute, subpart F of the Internal Revenue Code. The statute clearly shows age. What revisions should be considered in the name of international competitiveness?

The debate needs to be relaunched because, although there has been a great deal of recent discussion about subpart F, much of it has soared above and beyond the ostensible subject. It has approached subpart F from perspectives that are historical and perhaps oxymoronic (what was Congress *really* thinking in 1962?), economic (is capital export neutrality reconcilable with — or preferable to — capital import neutrality?), and philosophical (how can we best advance the cause of global welfare? U.S. welfare?). What happened to practical? That is where the debate should focus, and that is why Chairman Grassley's questions are so good. They portray what is at stake.

The questions imply, fairly, that the subpart F debate is really about tax havens. The statute does not impose a serious impediment to investment in, or income derived from, the high-tax countries that are the locus of most U.S. foreign investment, such as Germany, Japan, and the United Kingdom. An effective rate of 31.51 percent or higher puts income beyond the statute's reach. Subpart F may intrude in those countries at the margin, and perhaps occasionally more deeply, but the overall limitation on the foreign

